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Supreme Court of the United States

October Term, 1979
No. 79-1348

WORLDWIDE CHURCH OF GOD, INC., *et al.*,
Petitioners,

vs.

PEOPLE OF THE STATE OF CALIFORNIA,
Respondent.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

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Respondent.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

Statement of the Case.

Los Angeles Superior Court case No. C 267-607, entitled *The People of the State of California v. Worldwide Church of God, Inc., et al.*, was initiated January 2, 1979. That proceeding is primarily concerned with correcting alleged fraudulent diversion of assets of the Worldwide Church of God, Inc. (hereafter "Church"), Ambassador College, Inc. (hereafter "College") and Ambassador International Cultural Foundation (hereafter "Foundation") by individuals who control those corporations — particularly petitioner Stanley R. Rader. The action seeks to compel an accounting and further equitable relief shown to be warranted by the accounting. It was brought by the Attorney General of the State of California as the only party other than the accused wrongdoers having the clear legal standing under California law to do so. (See Argument at II A, p. 23 *infra*.)

The operative complaint, the Second Amended Complaint (P.App. 12b),[1] alleges that individual defendants have been and are syphoning off and diverting to their own use and benefit substantial sums which are assets of the Church, College and Foundation. Rader has admitted that he has engaged in specific self-dealing transactions with the charitable corporations. During a three day hearing (held January 10-12, 1979) to determine if the temporary receiver of the Church, College and Foundation should be replaced by a receiver *pendente lite*, Rader testified that he is an officer and director/trustee of each of the three nonprofit corporations; that he has acted as general counsel and as a certified public accountant for the three nonprofit corporations; that he has a lucrative employment contract with the church executed a time when he was acting for the Church in all those capacities, but that he knew of no independent legal advice which the church received before entering into that contract (R.App. 5-6);[2] that one or all of the nonprofit corporations paid for all or part of a Beverly Hills home the title to which Mr. Rader took in his own name and subsequently sold for 1.8 million dollars, pocketing the proceeds; that the Church purchased a home in Tucson, Arizona title to which was placed in Mr. Rader's name; that Mr. Rader organized and owned an interest in an advertising agency called Worldwide Advertising, Inc. which handled

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[1]References are to Appendices to the Petition for a Writ of Certiorari herein designated P.App., or to Appendices presented with this Brief In Opposition, designated R.App.

[2]Mr. Rader's employment contract dated July 30, 1976 was placed in evidence before Judge Title. (R.App. 70.) It shows that Rader was, and had been since at least 1969, and probably before, acting in a fiduciary capacity with the Church, College and Foundation. In connection with determining to confirm the appointment of the receiver the court stated " . . . I certainly question the legality of his present employment agreement, the enforceability of that present employment agreement with the church under these circumstances." (R.App. 24.)

all media time purchases for the Church, College and Foundation; and that Mr. Rader formed a partnership known as Mid-Atlantic Leasing, which has purchased airplanes and leased them to the charitable corporations for profit. (R.App. 7-21.)

Much of the evidence presented at that hearing had been presented in documentary form only nine days before to the Superior Court in support of the state's ex parte application for appointment of a temporary receiver.[3] Among other things, that documentary evidence included the following information:

1. In the "Pastor's Report" of August 14, 1978 (R.App. 46-48) Mr. Rader admitted to engaging in the various self-dealing transactions discussed, *supra*.

2. Mr. Rader's law firm acts as attorneys for all of the nonprofit corporate defendants. (R.App. 38.)

3. Documents entitled "Pastor General Department — Report of Expenditures" (Exhibit B to Declaration of Benjamin Chapman, R.App. 53) and a monthly executive expense analysis dated March 3, 1978 (Exhibit C to the Declaration of Alvin Earl Timmins, R.App. 60) set forth luxury expenditures by corporate executives in amounts so extravagant that Judge Julius M. Title, who presided at the hearing of January 10-12, 1979, referred to them as "astonishing." (R.App. 22.) (Discussed in more detail, *infra*.)

4. In July 1978, Mr. Rader sold for $1,800,000 the Beverly Hills home for which the Church had paid, pocketing the proceeds. (R.App. 41.)

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[3]The sworn declarations, and most of the exhibits thereto, which made up that documentary evidence are reproduced in R.App.D, pp. 35 to 69. Petitioners incorrectly characterize the hearing on the ex parte application, as a "secret meeting" (Petition, p.5). The hearing was recorded verbatim by a court reporter, and the transcript thereof is part of the record. (P.App. 156b.)

5. From May 1978 to the filing of this action the Church had liquidated or was in the process of liquidating 12 parcels of real estate for a total price in excess of 13 million dollars. (R.App. 61-62, 68.)

6. The declaration of Benjamin Chapman, a former director of the Church and College, revealed that as a director he had never voted on any question in connection with the management of those corporations, and that defendant Rader effectively controls the operation and management of Church finances. (R.App. 52, 54.)

7. A Church "Pastors Report" dated December 19, 1978 accuses defendants Wright and Kuhn of diverting Church assets to a Texas corporation owned by them. (R.App. 64.) A letter dated July 24, 1978, from defendant Rader to Garner Ted Armstrong, (a former high Church official and son of Herbert W. Armstrong) made elaborate offers of compensation and other benefits in exchange for a requested promise by Garner Ted Armstrong that he would not reveal the internal financial affairs of the Church. (Declaration of Alvin Earl Timmins, R.App. 61.)

8. Church employees had informed declarant Alvin Earl Timmins that many of the Church's records, particularly those pertaining to executive compensation and expense accounts, and to transactions between the Church and various entities owned and controlled by defendant Rader, had been removed from the Church's main office in Pasadena to the suite of offices maintained by Rader and his accounting firm (and his affiliated companies) in Century City, and that many records were being mechanically shredded or destroyed. (Declaration of Alvin Earl Timmons, R.App. 61.) The Executive Payroll for the Church and College were subsequently found on January 3, 1979 in the Century City offices of Worldwide Advertising, one of the entities controlled by Rader. (R.App. 17.) Also, a mechanical document shredder was found in the executive offices of Ambassador College on January 3, 1979. (R.App. 102, 104.)[4]

Testimony at the January 10-12, 1979 hearing further showed that some of the self-dealing transactions by Rader were continuing — *e.g.*, the Tucson home, airplane leases, and lucrative employment contract. In appointing the receiver *pendente lite*, Judge Julius M. Title concluded that ". . . there have been some very serious questions raised here concerning the use and transfer of assets in the form of money and property to those in control of the church." (R.App. 22.)

The complaint also seeks to correct the failure of Church, College and Foundation leaders to comply with the Church's own articles of incorporation and with State corporation laws. (A copy of the Articles of Incorporation is reproduced at R.App. 90 to 92.) It alleges that the Church incorporated under the California Nonprofit Corporation Law, which requires the corporation to be run by a board of directors, but that in fact all three corporations have "dummy" boards which exercise no powers at all. An order is prayed for directing the corporations to comply with the terms of their Articles of Incorporation and State laws under which they were organized. The Superior Court also may have been impressed by the fact that there existed at the time of the

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[4]On the basis of such information a Superior Court Judge determined that the immediate appointment of a receiver ex parte was necessary to bring an immediate halt to diversions of charitable trust assets and to safeguard the records of past diversions from destruction or loss. Thus there was probable cause to conclude that the immediate and ex parte appointment of a receiver was necessary in order to prevent irreparable injury to the public interest through the dissipation and diversion of charitable trust assets and the destruction or secreting of trust records evidencing such diversions. Under the circumstances nothing short of appointing a receiver to take possession of such financial records and to halt diversion of assets would have sufficed to prevent such irreparable injury.

January hearing three different versions of the By-laws of the church, differing from one another on crucial points. For instance, a provision was suddenly inserted at the time the state action commenced indemnifying officers and directors for expenses of defending actions for abuse of their fiduciary duties as trustees of these charitable assets. (See Article XII of By-laws R.App. 32 and R.App. 121-122.)

Again, in confirming the receivership, Judge Title expressed concern that the corporations were not being operated in compliance with their own articles of incorporation:

> "In spite of the fact there are specific provisions in the articles and by-laws which place control in the board of directors, it seems, nevertheless, to be conceded that for many years this was essentially a one man operation, with Mr. Armstrong making all the decisions on a completely unilateral basis . . ." (R.App. 23.)
>
> "Mr. Armstrong apparently has taken the position that he can do what he pleases with reference to the affairs of this church, and without consulting with anyone else, including the board of directors. When you combine this with the inference that Mr. Rader now in reality has replaced him or is in the process of replacing him it becomes obvious, it seems to me, that the trial court will have to make a full inquiry into this situation." (R.App. 25.)

But these were not the only concerns of the Superior Court in appointing a receiver pending trial. The church financial reports attached to the complaint disclose travel expenditures of bizarre and exorbitant amounts. For instance, credit card expenditures by Osamu Gotoh, an employee of the church, and a defendant in the state court

proceedings, exceeded $2 million in one three year period. Examples are the following: August 8, 1975 American Express, Hotel Plaza, Athenee, Paris $12,416.93; August 31, 1975 American Express, Imperial Hotel, Tokyo, Japan $13,735.74. June — September 1975 purchase of cameras and related equipment — totaling an excess of $10,000. Perhaps most astonishing of all was that these documents disclosed an unbelievable total of credit card expenditures by Gotoh for travel, lodging and "public relations" purposes of $813,931.53 in the period July 1, 1975 through June 30, 1976. (R.App. 39-41.)

But Mr. Gotoh was not alone in such expenditures. Mr. Rader made a charge (only one example of many) on September 11, 1975 to Diners Club at the Hotel Plaza, Athenee in Paris of $12,049.39. (R.App. 40.)

Evidence also showed that similar expenditures continued in 1978. Another church financial report attached to the original moving papers shows that Rader had incurred some $51,431.14 in expenses which were being held for payment in March 1978, including a $22,571.19 bill from Hotel Plaza, Athenee, Paris, and $10,591.17 in expenses relating to the Tucson home, including furnishing, mortgage payment and "golf club." The same report shows $51,094.13 in travel expenses incurred by Henry Cornwall, another defendant in the State court proceedings, including $22,-925.56 at the "Imperial Hotel." (R.App. 40-41.)

There was also substantial evidence from which Judge Title could conclude that records had been removed from church premises after the initial appointment of the receiver (January 2, 1979) and in violation of court order. Despite his emphatic denials, there was substantial evidence that John Kineston (Rader's chauffeur and administrative assistant) had removed church records from church premises after the receiver was appointed. (R.App. 112-113.) Like-

wise, although Virginia Kineston (Rader's executive secretary) had filed a declaration denying that shredding of church records had ever taken place, substantial evidence was produced to show that such shredding had in fact taken place, and Mrs. Kineston herself ultimately admitted it. (R.App. 101-105.)

Judge Title confirmed the original appointment of a receiver *pendente lite* first orally on January 12, 1979, and subsequently in a written order dated January 19, 1979. (P.App. 41b.) That order provided that the receiver was to supervise and to monitor only the business and financial operations of the Church and conduct an audit thereof. He was ordered not to interfere even with those business and financial operations except to the extent he believed it necessary to protect assets from continuing misappropriation. Thus the Court carefully tailored the receivership to accomplish the narrow purposes of securing a financial audit, safeguarding financial records and preventing any continuing misappropriation of funds. The receiver was instructed not to interfere with the ecclesiastical functions of the Church. He was given the right to fire employees of the Church but not to affect their standing as Church members. The Court assiduously sought to avoid any interference in matters of religious doctrine and practice.

At that time, and during the entire term of the receivership, petitioners asserted to the Court that the chief objectives of the receivership, to secure an accounting and safeguard assets, could be achieved through injunctive orders "with which defendants (petitioners herein) assured the court they would comply." (R.App. 92.) Upon motion of the petitioners to dissolve the temporary receivership, having received these assurances from the petitioners, the trial court on March 2, 1979 dissolved the receivership and substituted an injunctive order (P.App. 49b). The court reserved

jurisdiction to reinstitute the receivership if that proved necessary to protect charitable assets and secure a proper accounting from the petitioners.

Such reservation of jurisdiction to reinstitute the receivership indeed proved to be necessary when the petitioners repudiated their assurance of cooperation with the injunctive order, filed an appeal from that order, and asserted that all mandatory aspects of the injunctive order were stayed pursuant to California law pending appeal. The court on its own motion thereupon reinstituted the receivership by its Minute Order of March 12, 1979 (P.App. 59b) asserting that "the *status quo* of the assets and records must be maintained pending appeal." However, the order further provided that reinstatement of the receivership would be stayed if petitioners posted a $1,000,000 appeal bond. Appellants then posted such a bond.

In arguing against the reinstitution of the receivership, petitioners' counsel asserted that the audit could still go forward through discovery in the form of depositions, interrogatories, production of documents, etc., as those procedures would not be stayed by appeal from the March 2, 1979 order. (R.App. 87.) Obviously, petitioners have by their subsequent conduct repudiated that position. Here they ask this Court to foreclose even discovery as an avenue to ascertain the extent of their own wrongdoing.

Subsequent to the stay of the receivership, the primary focus of the state court proceedings has revolved around discovery. Attempts thus far futile, to obtain discovery from the petitioners, include the discovery orders which are the subject of the pending Petition for Writ of Certiorari (Petition, pp. 2-3, n. 3).[5]

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[5]Another such order, one which was the subject of a prior unsuccessful petition for certiorari (No. 79-205, denied October 15, 1979), instructed Rader to appear for his deposition, initially in January 1979. He eventually appeared, but refused to answer virtually every question propounded (R.App. 95).

While petitioners have given the State virtually no discovery, they have obtained extensive discovery from the State and from third party witnesses without interference from the State (P.App. 244b). Such discovery (obtained prior to July 6, 1979) includes production of documents from the State on June 29, 1979, receipt of a list of all Church documents in the State's possession, seven depositions, and production of General Telephone Company records and documents. All depositions taken by the petitioners have been adjourned without opportunity for the State to examine the witnesses. (R.App. 93-95.)

Because of the priority given to the State to take Mr. Rader's deposition, for which he repeatedly refused to appear (P.App. 276b), because no State court defendant (petitioners herein) has made any discovery to the State, because all defendants have made it clear that they would refuse to make discovery at least until appellate reviews of discovery orders were complete, because petitioners had obtained substantial discovery both from third parties and from the State, and out of ''elemental fairness,'' the Superior Court stayed all discovery by defendants commencing August 8, 1979. (P.App. 281b.) As the Court stated on September 21, 1979, in extending the stay until November 26, 1979, he did so not to punish other defendants for Mr. Rader's actions but because no defendants were making discovery and in fact openly stated they would make no discovery (R.App. 88-89).[6]

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[6]Petitioners argue that the Superior Court's stay of their discovery from the State is a form of punishment for seeking appellate review of its orders compelling petitioners to make discovery to the State. (Petition, p. 44.) This argument ignores the fact that petitioners were allowed to conduct the extensive discovery described in the text, *supra*, without the State's having received any discovery from them whatsoever. In fact Petitioners are not being denied *reciprocal* rights of discovery, as was the defendant in *Wardius v. Oregon* (1972) 412 U.S. 470, for they have not yet reciprocated. That case merely held ''[I]t is fundamentally unfair to require a defendant to divulge the details of his own case while subjecting him to the hazard of surprise concerning refutation of the very pieces of evidence which he disclosed to the State.'' *Id.* at 476.

Moreover, the stay serves the rational policy of avoiding a waste of both charitable and State resources in propounding and responding to discovery until it has been judicially determined whether in fact the State will be allowed to proceed, not only with its own discovery, but with its very case. Petitioners do not (and cannot) argue that they will be forced to trial without the benefit of adequate discovery.

Summary of Argument.

Petitioners' key contentions are that the challenged pretrial discovery orders are constitutionally defective because (1) the very filing and prosecution of the lawsuit of which they are a part violates petitioners' First Amendment rights; and, (2) there is a First Amendment requirement that before the instant discovery will be permitted from a religious organization in an action to remedy ''misuse of church assets by individual church officers'' there must be a ''judicial determination that the suspicion has some basis in fact.'' (Petition, p. 11.)

Respondent contends to the contrary as follows:

(1) This Court should not interfere with the state court discovery proceedings because there has been no showing that petitioners are not receiving adequate opportunity to vindicate their constitutional concerns in the state courts, because the discovery orders under attack are merely pretrial orders designed to facilitate the trial, and because no showing has been made that the state courts cannot sort out the myriad legal and factual issues presented by the proceedings;

(2) The instant suit is brought for the purpose of furthering a compelling state interest in providing a remedy, through the application of neutral principles of law, for fraudulent diversion of the assets of religious and charitable corporations and violation of the articles of such corporations, pursuant to the state's well settled powers to enforce

charitable trusts and state corporation laws; the suit does not have the effect of materially inhibiting any legitimate religious practice; and to the extent that any religious practice may be marginally affected, such is clearly necessary to further the above compelling state interests;

(3) If discovery obtained from a religious organization is necessary to further such compelling state interests, it need not be justified by any further showing; and to the extent such a showing may constitutionally be required respondent has produced it in ample measure through extensive evidence in the trial court of *prima facie* violations of state fiduciary and corporation laws; significantly, petitioners do not argue that the self-dealing transactions proved by the state do not constitute *prima facie* violations of state law fiduciary standards; it is therefore difficult to discern the basis for their claim that this lawsuit "is essentially a fishing expedition." (Petition p. 29.)

ARGUMENT.

I.

Principles of Federalism Require the Court to Abstain.

A review of a lower federal or state court decision on a writ of certiorari is not a matter of right, but of sound judicial discretion. The writ should be granted only when there are special and important reasons therefor. (28 U.S.C. Rules of the Supreme Court, Rule 19; *Durham v. United States* (1971) 401 U.S. 481, 483).

In exercising that discretion over the years, this Court has given recognition to various circumstances under which a federal court may decline to proceed with a review of a state court decision even though it has jurisdiction under the Constitution and statutes. This practical concept, generally referred to as the "abstention doctrine," cautions federal courts to stay the exercise of their power to review and assess state statutes in situations (1) where the case involves difficult and unsettled issues of state law which, if first decided by the state courts, might avoid the necessity for the federal courts to decide the asserted federal constitutional claims, (2) where there might be needless conflict with the administration by a state of its owns affairs, and (3) where decision in a diversity case turns upon difficult and unresolved questions of state law. (R. Stern & E. Gressman, Supreme Court Practice 101-103 (5th ed. 1978); C. Wright, Law of Federal Courts § 52 (3d ed. 1976); *see also* L. Tribe, American Constitutional Law §§ 3-39 to 3-41 (1978).) In the recent landmark case of *Younger v. Harris* (1971) 401 U.S. 37, Justice Black, speaking for the Court, described the doctrine as one of comity:

> ". . . that is, a proper respect for State functions, a recognition of the fact that the entire country is made up of a Union of separate state governments, and a

continuance of the belief that the National Government will fare best if the States and their institutions are left free to perform their separate functions in their separate ways. This, perhaps for lack of a better and clearer way to describe it, is referred to by many as 'Our Federalism'. . . ." (*Id.* at 44.)

This Court's most recent exposition on abstention is found in *Moore v. Sims* (1979) .... U.S. ...., 60 L.Ed.2d 994, 99 S.Ct. 2371. In *Moore*, authorities of the State of Texas had initiated proceedings in state court to take custody of three minor children who were suspected of being the victims of child abuse. The parents brought suit in the federal district court to challenge the constitutionally of the state statutory scheme under which the Texas authorities were proceeding. A three-judge district court concluded that abstention was unwarranted, granted appellants relief, and enjoined further state proceedings. This Court noted probable jurisdication and reversed, holding that the district court should have abstained. The following language from *Moore* applies with equal force to the case at bar:

"The *Younger* doctrine, which counsels federal court abstention when there is a pending state proceeding, reflects a strong policy against federal intervention in state judicial processes in the absence of great and immediate irreparable injury to the federal plaintiff. *Samuels v. Mackell*, 401 U.S. 66, 69 . . . (1971). That policy was first articulated with reference to state criminal proceedings, but as we recognized in *Huffman v. Pursue, Ltd.*, 420 U.S. 592 . . . (1975), the basic concern — that threat to our federal system posed by displacement of state courts by those of the National Government — is also fully applicable to civil proceedings in which important state interests are involved. . . . The existence of these conditions [that is,

where the state is a party to the state proceeding, and where the state statute in controversy is 'in aid of and closely related to criminal statutes'], or the presence of such other vital concerns as enforcement of contempt proceedings, *Juidice v. Vail*, 430 U.S. 327 . . . (1977), or the vindication of 'important state policies such as safeguarding the fiscal integrity of [public assistance] programs,' *Trainor v. Hernandez*, 431 U.S. 434, 444 . . . (1977), determines the applicability of *Younger-Huffman* principles as a bar to the institution of a later federal action." (*Id.* at 2377.)

This Court then set forth the policy reasons underlying the abstention doctrine as follows:

"There are three distinct considerations that counsel abstention when broad-based challenges are made to state statutes, and it is common to see each figure in an abstention decision; for the broader the challenge, the more evident each consideration becomes. There is first the *Pullman* concern: that a federal court will be forced to interpret state law without the benefit of state court consideration and therefore under circumstances where a constitutional determination is predicated on a reading of the statute that is not binding on state courts and may be discredited at any time — thus essentially rendering the federal court decision advisory and the litigation underlying it meaningless. [Citations.] These dangers increase with the breadth of the challenge.

"The second consideration is the need for a concrete case or controversy — a concern also obviously enhanced by the scope of the challenge. . . .

"The final concern prompted by broad facial attacks on state statutes is the threat to our federal system of

government posed by 'the needless obstruction to the domestic policy of the states by forestalling state action in construing and applying its own statutes.' [Citation.]

"State courts are the principal expositors of state law. Almost every constitutional challenge — and particularly one as far ranging as that involved in this case — offers the opportunity for narrowing constructions that might obviate the constitutional concerns and state interests. When federal courts disrupt that process of mediation while interjecting themselves in such disputes, they prevent the informed evolution of state policy by state tribunals. *Trainor v. Hernandez*, 431 U.S. 434, 445, . . . (1977). *The price exacted in terms of comity would only be outweighed if state courts were not competent to adjudicate federal constitutional claims — a postulate we have repeatedly and emphatically rejected. Huffman, supra*, 420 U.S., at 610-611. . . .

"In sum, the only pertinent inquiry is whether the state proceedings afford an adequate opportunity to raise the constitutional claims." (*Moore v. Sims, supra*, at 2380-2381. Emphasis added.)

In the underlying state action here at issue, the State of California, acting through its Attorney General, has brought an action to safeguard the assets of various charitable nonprofit corporations from fraudulent misappropriation by the persons in control thereof.[7]

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[7]In his recent treatise on constitutional law, Professor Lawrence Tribe has set forth five rules to describe the abstention doctrine, the third of which is peculiarly applicable to the case at bar:

"(3) If, at the time the litigant initiates federal proceedings, the litigant is a party in a state civil proceeding initiated by state officials, and if the litigant can raise the constitutional issue in that proceeding, the litigant will again ordinarily be denied federal declaratory or injunctive relief." L. Tribe, American Constitutional Law § 3-41 (1978).

By this action the state seeks to vindicate its strong and legitimate public policies (1) against fraud and misappropriation, (2) that charitable assets be applied to charitable purposes, and (3) that the officers and directors of any corporation formed under state law operate that corporation in accordance with its articles of incorporation. Clearly, safeguarding the fiscal integrity of nonprofit corporations holding assets upon a charitable trust is no less important than safeguarding the fiscal integrity of public assistance programs; thus, the issues pending in the underlying state action are of "vital state concern." (*Trainor v. Hernandez* (1977) 431 U.S. 434, 444.) Moreover, petitioners have not, and cannot, make any showing that the underlying state action was brought in bad faith or for purposes of harassment, nor that either of the state statutes which they seek to call into question (former Calif. Corp. Code § 9505 and its successor, Calif. Corp. Code § 9230 — P.App. 30a-32a) is "flagrantly and patently violative of express constitutional prohibitions in every clause, sentence and paragraph, and in whatever manner and against whomever an effort might be made to apply it." (*Huffman v. Pursue. Ltd.* (1975) 420 U.S. 592, 611.)

Respondent submits that in light of the foregoing principles, abstention is not only clearly applicable in the instant case, it is mandatory. For this Court to interject itself into this matter at this early stage of the proceedings would be a clear and direct abrogation of the principles of Federalism.

II.

Neither the State Court Proceeding nor the Discovery Orders Under Attack Violate the First Amendment.

A. Pursuant to Ancient and Settled Legal Principles, Religious Organizations Hold Their Assets in Trust for Their Religious Purposes, Which Are Also Charitable Purposes, and the State Attorneys General Are the Only Parties With Clear Practical and Legal Standing to Enforce Such a Trust.

In general throughout the United States, religious purposes are regarded as charitable, and trusts for religious purposes are enforced as charitable trusts. (See *In Re Metropolitan Baptist Church of Richmond, Inc.* (1975) 48 Cal.App.3d 850; IV Scott on Trusts (3d ed.) § 371, pp. 2879, 2880; *Morman Church v. United States* (1889) 136 U.S. 1, 47, 51, 62.) Likewise, the state attorneys general are charged with the enforcement of such trusts because the fulfillment of the purposes of charitable, including religious, organizations is thought to be of general benefit to society as a whole.[8] In that sense, such entities are trustees of their assets and hold such assets in trust for the religious or charitable purposes set forth in their governing documents. (*Pacific Home v. County of Los Angeles* (1953) 41 Cal.2d 844, at 851-852; *In Re Metropolitan Baptist Church of Richmond, Inc.* (1975) 48 Cal.App.3d 850, 857. See also *Morman Church v. U.S., supra,* at 51.) Any diversion of such funds is a breach of trust. (See California Civil Code §§ 2228 et seq.; *In Re Metropolitan Baptist Church of Richmond, Inc., supra,* at 857; *Holt v. College of Osteopathic*

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[8]In California the Attorney General's standing is codified at former Corporations Code section 9505; replaced as of January 1, 1980 nearly verbatim by Corporations Code §§ 5250 and 9230. See P.App. 30a through 32a for the text of former section 9505 and current section 9230, respectively.

Physicians & Surgeons (1964) 61 Cal.2d 750, at 759-760; *People v. Christ's Church* (1947) 79 Cal.App.2d 858; *People of the State of Cal. v. Larkin* (N.D. Cal. 1976) 413 F.Supp 978.)

In *Morman Church v. United States, supra,* this court held that the assets of "public or charitable corporations" upon dissolution "become subject to the disposal of the sovereign;" and that the Morman Church corporation was subject to that rule. (*Id.* at 47.) In that case Congress had revoked the charter of the church corporation, which had been formed under the laws of the Federal Territory of Utah. The government brought suit ". . . for the purpose of taking possession of and holding for final disposition the property of the defunct corporation in the hands of a receiver, and winding up its affairs." (136 U.S. at 64.)

> "This Court upheld the revocation of the charter, relying on the reserved power of the Congress over the acts of territories, 136 U.S., at 45-46. The seizure of the property was bottomed on the general rule that where a charitable corporation is dissolved for unlawful practices, *id.*, at 49-50, the sovereign takes and distributes the property according to the *cy pres* doctrine to objects of charity and usefulness, e.g., schools. *Id.*, at 47, 50-51. A failure of the charitable purpose could have the same effect. *Id.*, at 59." (*Kedroff v. St. Nicholas Cathedral* (1952) 344 U.S. 94, 120.)

The court applied a "leading and prominent principle" of the "law of charities" to ensure "that property devoted to a charitable and worthy object, promotive of the public good, shall be applied to the purpose of its dedication, and protected from spoilation and diversion to other objects. Though devoted to a particular use it is considered as given

to the public, and is, therefore, taken under the guardianship of the laws.'' (136 U.S. at 51.)

In more recent time this Court has continued to recognize that the activities of religious organizations are of general benefit to society as a whole, and has on that basis held that a state grant of property tax exemption to churches does not violate the establishment clause of the First Amendment. (*Walz v. Tax Commission* (1970) 397 U.S. 664, 680.) In discussing the public benefit aspects of religious and other charitable organizations which justify extending to them such tax exemption, Chief Justice Burger, speaking for the Court, observed:

> ''New York, in common with the other States, has determined that certain entities that exist in a harmonious relationship to the community at large, and that foster its 'moral or mental improvement,' should not be inhibited in their activities by property taxation or the hazard of loss of those properties for nonpayment of taxes. . . . The State has an affirmative policy that considers these groups as beneficial and stablizing influences in community life and finds this classification useful, desirable, and in the public interest.'' (397 U.S. at 672-673.)

See also the separate concurring opinions of Justices Brennan (397 U.S. at 687) and Harlan (397 U.S. at 696-697).

It follows that the State has a strong interest in preventing and correcting the fraudulent misappropriation of the assets of religious entities. The purposes of the Worldwide Church of God include secular public benefit activities. The separate, but church controlled, College and Foundation corporations are formed for educational and cultural purposes which are clearly not purely religious. Moreover, the church

receives significant contributions from members of the public outside the church membership.[9]

Enforcement by the various state attorneys general of charitable (including religious) trusts is an ancient and nearly universal practice in this nation. Such a practice must not lightly be cast aside on constitutional grounds. As Chief Justice Burger observed in *Walz, supra*:

> ''Yet an unbroken practice of according the [tax] exemption to churches, openly and by affirmative state action, not covertly or by state inaction, is not something to be lightly cast aside. Nearly 50 years ago, Mr. Justice Holmes stated: 'If a thing has been practiced for two hundred years by common consent, it will need a strong case for the Fourteenth Amendment to affect it. . . .' '' (397 U.S. at 678.)

The supervision of charity by state attorneys general goes back far longer than even 200 years. The attorneys general and chancery courts of England had such supervisory powers prior even to the enactment of the English Statute of Charitable Uses in 1601. (Stats. 43 Elizabeth I, c. 4; IV Scott on Trusts (3d ed.) § 368.1, p. 2857, § 391, p. 3002.)

Most recently, Mr. Justice Rehnquist has refused to halt a state court action by respondent herein to remedy fraudulent diversion of assets of another religious corporation in *Synanon Foundation, Inc., et al. v. The State of California. et al.* (1980) ..... U.S. ..... , 100 S.Ct. 497 . There, Justice Rehnquist refused the application of a religious organization for a stay of an order of the United States District Court for the Eastern District of California denying appli-

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[9]These facts were specifically admitted by Petitioners in their prior petition to this Court last term (No. 78-1720). See pp. 4-5 of that petition, of which this Court is respectfully requested to take judicial notice.

cants' motion for a preliminary injunction forbidding the State of California and its Attorney General from instituting a civil action against the applicants in state court. The only substantive difference between the relief sought in the two cases is that in *Synanon, supra,* the applicants sought an order prohibiting the *commencement* of a state court action, while in the instant case the petitioners seek to overturn state court discovery orders on the asserted basis that the entire action is unconstitutional and without which the action cannot for all practical purposes *continue* to proceed.

In the *Synanon* case, *supra,* Justice Rehnquist noted that:

> "The District Court's opinion denying the prayer for a preliminary injunction indicates that the Attorney General of California has the traditional power of the chief law enforcement officer of most jurisdictions to intervene in the administration of charitable trusts or corporations when he has reason to believe that they are not being administered in accordance with the trust instrument or in contravention of state law." (100 S.Ct. at 497.)

Justice Rehnquist went on to hold that state courts are free to resolve property disputes concerning hierarchical churches in accordance with neutral principles of law. In that regard, his opinion states as follows:

> "Applicants contend, however, that by reason of the fact that they are a church, under the First and Fourteenth Amendments of the United States Constitution they are somehow entitled to different treatment than that accorded to other charitable trusts. But we held only last term that state courts might resolve property disputes in which hierarchical church organizations were involved in accordance with 'neutral principles' of law. *Jones v. Wolfe,* 47 U.S.L.W. 4962, 4963-64 (1979); *Presbyterian Church v. Hull Church,* 393 U.S. 440, 449 (1969)." (100 S.Ct. at 497.)

Clearly, the *Synanon* case supports the State's position that the First Amendment does not bar the instant state court civil action seeking to remedy fiscal fraud in the administration of charitable assets held by a church and related corporations.

In California and in many other states the attorney general is the only party other than corporate directors or trustees (who in this case are the very persons accused of wrongdoing) who has standing to enforce a charitable trust. (*Holt v. College of Osteopathic Physicians & Surgeons, supra,* at 755-757; IV Scott on Trusts (3d ed.) § 391, p. 3002 at 3006.). While the public as a whole is the beneficiary of all charitable trusts, members of the public (including in this case members of the Worldwide Church of God) have no clear authority to bring court actions to enforce a charitable trust.[10] If petitioners are successful in their contention

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[10]Under the new California Nonprofit Corporations Code, effective January 1, 1980, standing to bring an action to remedy a breach of trust by a person(s) in control of a religious corporation is specifically limited to the corporation itself, officers and directors of the corporation or persons with a reversionary, contractual or property interest in the assets subject to trust. (Corp. Code § 9142.) Members, whether congregants or donors, are not included. Thus outright breach of trust, such as diverting assets to private inurement, is not subject to redress by members of the affected church.

Standing to correct another form of trust abuse, self-dealing, is given to "members" (§ 9243) but the term "members" is so defined and the requisites of standing so rigid as to effectively eliminate standing for most church members, including members of the petitioner Church.

"Member" is defined by section 5143 of the new code to mean ". . . any person who has the right to vote for the election of director or directors of a corporation pursuant to the corporation's articles or bylaws." Under the Bylaws of the petitioner Church, the only person given authority to appoint directors of the corporation is the President, Herbert W. Armstrong. (See, art. IV, § 2 of the Bylaws R.App. 29.) Therefore, Church members are not "members" of the Corporation. Nor are other persons, including members and congregants, given authority by the Bylaws to bring such actions. Moreover, even if members

(footnote continued on following page)

that the Attorney General can likewise not pursue such an action, it would merely legitimize fraud in the name of religion. This Court should have no trouble rejecting such a lawless result.

Petitioners suggest that "permitting derivative suits by individual church members" (Petition p. 24) would be a sufficient alternative for "pursuing probable misappropriation or other misconduct by individual church officers" (Petition p. 23) which would presumably be less intrusive of First Amendment interests than the course pursued here. Besides being contrary to the long tradition of state enforcement of charitable trusts, that approach would require government to leave to private parties the task of vindicating compelling state interests. Respondent knows of no case holding that such would either be wise public policy or required constitutional doctrine. For one thing, private plaintiffs may be tempted to sacrifice the public interest which they represent in favor of their own private interests should the two conflict. For another, private plaintiffs may lack the resources in many instances to litigate successfully against a corporate management with other people's money at its disposal.[11]

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of this or any church qualify under the new code to bring an action to correct self-dealing, by its own terms section 9243 requires compliance with the provisions of another section, section 5710, which requires such a member to provide security in an amount up to $50,000 upon defendant's motion and a specified showing, excepting where the action is brought by a large number of members, 100 or as otherwise provided dependent on the number of persons with "voting power." In the case of Worldwide Church of God, of course, the electorate consists only of one man, Herbert W. Armstrong.

[11]A case in point is the instant one in which prior to this petition respondent has (successfully so far) withstood over 15 petitions for extraordinary writs and two appeals brought by petitioners in state appellate courts, as well as two prior petitions for certiorari and five applications for stays in this Court, and three counter-suits (*Lopez v. State*, L.A. Superior Court No. C276 767; *Worldwide Church of God, et al. v. State*, L.A. Superior Court No. NE C 27165; and *Worldwide Church of God v. State*, U.S. District Court, Southern District of California, No. 79-0183).

Moreover, such a derivative suit would necessarily involve courts in making the same types of decisions and ordering the same types of discovery as in the instant case. Since the judiciary is as much an arm of government as the executive, such a suit would include "intrusions" comparable to the ones of which petitioners here complain. See *Barr v. United Methodist Church* (1979) 90 Cal.App.3d 259; a suit brought by private plaintiffs against a church in which defendant argued (unsuccessfully) that the First Amendment prohibits making a church a defendant in a suit for fraud and breach of contract stemming from charitable activities carried on by church agents.

Finally, since the number of potential plaintiffs who could initiate such derivative suits could be quite large, that alternative carries the potential for multiplying the number of nuisance suits against churches, in each one of which the courts may have to make decisions and grant discovery comparable to those in the instant case.

B. The First Amendment Does Not Excuse the Perpetration of Fiscal Fraud in the Name of Religion, nor Does It Shield the Perpetrators From Corrective Action in the Courts.

Appellants' arguments that the Attorney General's efforts in this action to uncover and correct misappropriation of charitable funds somehow impedes impermissibly the free exercise of religion are grounded in the premise that the courts will never be able to distinguish successfully between the financial and business affairs of the church on the one hand, and its spiritual and ecclesiastical affairs on the other. The essence of such an argument is that the business and financial activities of a church at every level are inextricably intertwined with its religious activities and the fulfillment of its religious purposes, that it is impossible for the state to separate the secular activities of the church from its re-

ligious activities, and that *any* state supervision of the church's secular activities is therefore unconstitutional. The acceptance of such an assertion would necessarily lead to the conclusion that the state is simply powerless to correct any misuse of church assets by those in control of the church, no matter how wrongful or fraudulent it may be, because *anything* that such persons may do with church property would be, by definition, a protected religious activity.

That assertion notwithstanding, however, the law is not such an ass as to be unable to distinguish between secular matters (including fiscal fraud) and ecclesiastical belief. In *Cantwell v. Connecticut* (1940) 310 U.S. 296, while invalidating a conviction for alleged unlawful solicitation of funds for religious purposes, the United States Supreme Court nevertheless made it plain that "[n]othing we have said is intended even remotely to imply that, under the cloak of religion, persons may, with impunity, commit frauds upon the public." (310 U.S. at 306.)

The United States Supreme Court has also made it clear that the rule prohibiting "entanglement" between church and state does not apply to cases involving "fraud, collusion, or arbitrariness." (See, e.g., *Gonzales v. Roman Catholic Archbishop* (1929) 280 U.S. 1, 16; *Md. & Va. Churches v. Sharpsburg Ch.* (1970) 396 U.S. 367, concurring opinion of Brennan, J., fn. 3, at 369.)

Even Justice Douglas, as staunch an advocate of religious freedom as has sat on this Court in recent times, observed succinctly that he had no intention of intimating or suggesting "that any conduct can be made a religious rite, and by the zeal of the practitioners swept into the First Amendment." (*Murdock v. Pennsylvania* (1943) 319 U.S. 105, 109.)

Petitioners argue that the state court proceeding at issue here necessarily entails an unconstitutional entanglement of church and state, citing cases invalidating various governmental regulatory schemes which have been held to constitute a prior restraint on religious practices, and which were not supported by compelling governmental interests. (Petition, p. 27.) There is a most significant distinction, however, between such government regulation and what is happening in this case. The complaint in the instant case alleges that fraudulent acts have already occurred; namely, the diversion of church assets to private benefit. It does not seek to impose a regulatory scheme upon churches. That distinction is an important one because none of the cases cited by the petitioners to this Court have involved a suit to correct past and on-going fiscal fraud in the administration of a religious entity.

For example, *Surinach v. Pesquera de Busquets* (1st Cir. 1979) 604 F.2d 73 involved continuing close governmental regulation of the tuition prices charged by religious schools, which was not supported by a compelling state interest. In the instant case, on the other hand, the governmental action which grieves petitioners is not close and continuing regulation, but a single lawsuit addressed to fraudulent acts *which have already taken place* and are continuing. And the governmental interest which supports that lawsuit is the compelling interest in the prevention and correction of fraudulent misappropriation of assets dedicated to religious and charitable purposes. It cannot seriously be argued that the prevention of fraud is not a compelling state interest.

Likewise, other cases cited by petitioners are distinguishable from the instant case as involving governmental regulatory schemes which place direct prior restraints upon religious practices: *NLRB v. Catholic Bishop of Chicago* (1979) 440 U.S. 490 (invalidated federal agency's attempt

to regulate church school-teachers' activities); *Fernandes v. Limmer* (1979) 465 F.Supp. 493 and *Intern. Soc. for Krishna Consciousness v. Bowen* (7th Cir. 1979) 600 F.2d 667 (invalidated permit requirement for solicitation of funds).

Finally, in *Cantwell v. Connecticut* (1940) 310 U.S. 296,[12] the fountainhead of these cases, the court invalidated a criminal conviction for solicitation of funds for religious purposes without a required permit, clearly a prior restraint upon what has been long recognized as a legitimate religious practice, the solicitation of funds.

C. The Instant Action to Halt and Correct the Fraudulent Diversion of Charitable Assets Does Not Materially Burden Any Genuine Religious Practice; Any Incidental Burden Thereon Is Justified by Compelling State Interests.

The instant action, and the discovery orders attacked by petitioners, do not materially interefere with any genuine religious practice. Any incidental interference is necessitated by compelling state interests.

This Court first articulated the three-factor test it uses to examine free exercise claims in *Sherbert v. Verner* (1963) 374 U.S. 398. In that case, a Seventh-Day Adventist was denied unemployment insurance compensation because she refused to work on Saturday, the Sabbath of her faith. In order to analyze her claim that the denial of benefits in-

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[12]Neither do the *Cantwell or Intern. Soc. for Krishna Consciousness* cases, *supra* restrict state action to redress fraudulent diversion of charitable assets to criminal proceedings, as petitioners suggest (Petition, p. 30). See *Sec. & Exchange Com'n v. World Radio Mission, Inc.* (1st Cir. 1976) 544 F.2d 535 and *People v. Whitney* (1953) 121 Cal.App.2d 515. Moreover, search warrants and subpoenas available in criminal proceedings are just as obtrusive as civil discovery devices. *In Re Rabbinical Seminary, Etc.* (E.D.N.Y. 1978) 450 F.Supp. 1078, 1085-1086.

fringed on her free exercise of religion, the Court inquired: (1) Is a sincere religious interest at issue? (2) To what extent has the state interfered with that interest? (3) Is there a compelling state interest which justified the interference? In weighing "the seriousness of the individual deprivation against the governmental interests involved," the Court found that Mrs. Sherbert's First Amendment rights had been unconstitutionally abridged. (*Conservatorships and Religious Cults. Divining a Theory of Free Exercise* (1978) 53 N.Y.U.L. Rev., 1247, 1261.)

Nine years later in *Wisconsin v. Yoder* (1972) 406 U.S. 205, the court refined this balancing approach in a challenge by Amish parents to compulsory school attendance past the age of sixteen. The Court stated that in order to compel attendance it would have to be shown "either that the state does not deny the free exercise of religious belief by its requirement, or that there is a state interest of sufficient magnitude to override the interest claiming protection under the Free Exercise Clause." (*Id.* at 214.) "[In] essence . . . only those interests of the highest order and those not otherwise served can overbalance *legitimate* claims to the free exercise of religion." (*Id.* at 215, emphasis added.) Because the state action was in conflict with a central tenet of the Amish faith and because the state interest (in a citizenry adequately prepared for life) was served by the vocational education of the Amish themselves, the Court held that the state could not, on First Amendment grounds, compel school attendance.

Application of this three-factor test to the instant case clearly reveals that the state court civil fraud action does not directly interfere to any significant extent with any genuine religious interest, and that any incidental interference with such religious interests is far outweighed by compelling state interests.

The state suit is not directed at any religious doctrine or practice. Its principal purpose is to obtain an accounting of assets which have been fraudulently diverted from charitable purposes to private benefit; even the petitioners make no claim that such diversion is permitted by any church doctrine or practice. Moreover, such an accounting is necessary to advance the compelling governmental interest in the correction of fraud by ascertaining the extent of such fraud.

The state action is aimed exclusively at fiscal activity. It has been held that fund raising by a religious organization through the operation of a retail sales business is not a religious but rather a commercial activity which may constitutionally be licensed by the state. (*Muhammad Temple of Islam v. City of Shreveport, La.* (1974) 387 F.Supp.1129, aff'd. 517 F.2d 922 (5th Cir. 1975).) The court recognized that to the extent that the business profits were impeded by governmental licensing and regulation, the religious activities would be impeded by lack of funds. But the burden was an indirect one and justified by a legitimate state interest. If fund raising through the operation of a business is not a religious activity then *a fortiori* the fraudulent diversion of charitable assets held by a religious organization is not a religious activity either. If in correcting such fraudulent activity the state indirectly burdens legitimate religious activities then that burden is justified by a proper state interest. Logically, under the three-pronged test, if a religious interest is only indirectly affected by state action, the countervailing governmental interest which is served by such action need not be as strong in order to outweigh it as it would to justify direct infringement of a religious practice.

The fiscal fraud at which the instant suit is aimed is clearly no part of any religious practice. Only that activity which is actually religious in nature is favored with First Amendment protection. See, e.g., *Sec. & Exchange Com'n v.*

World Radio Mission Inc., supra, 544 F.2d 538. There, the S.E.C. brought an action to enjoin a religious organization and its leader from violating anti-fraud provisions of the 1933 and 1934 Securities Acts through false representations in connection with the solicitation of loans. Defendants asserted that even if such solicitations were untrue, and such loans were securities, they were entitled to First Amendment protection because "the 'investor' also, in effect, subscribes to religious 'articles of faith.' " But the court looked behind that assertion and found that the solicitation primarily offered the promise of high pecuniary returns rather than spiritual dividends. (*Id.* at 539.)

But even assuming for the sake of argument that petitioners have identified a significant religious interest which will be harmed by the instant state action, that action is not necessarily constitutionally infirm. Rather, the balancing test set forth in *Wisconsin v. Yoder* and *Sherbert v. Verner, supra*, is applicable thereto. The issue then becomes whether the infringement upon religious activities is outweighed by a substantial and important secular state interest. As discussed above, the State's interest in preventing and correcting fiscal fraud is not only strong and legitimate, but compelling; and where a corporation is controlled by those accused of defrauding it, an action for an equitable accounting, as in the instant case, constitutes an appropriate state action necessary to advance that compelling interest.

While Mr. Justice Rehnquist's opinion in *Synanon, supra*, is dispositive of the question in any event, this case does not involve an issue as to the State's general "investigative powers" over religious organizations, because the state action complained of by petitioners (discovery orders) are not part of an executive investigation, but part of a court suit. Such lawsuit necessarily involves the court as an impartial arbiter of the state's claims of wrongdoing, and the

judiciary rather than the executive makes the determination of what documents and testimony the executive will be permitted to elicit in the course of the lawsuit. Ultimately, the court decides whether the executive has adequately proven his allegations and if so, what judicial remedies will be applied.

Neither does this case involve the issue of whether the state can compel a church to account to it whenever it pleases (Petition, p. 34). Such a power is not necessary to confer standing upon the Attorney General to bring a suit to remedy fraudulent diversion of church assets. Paragraph 10 of the Second Amended Complaint (P.App. 16b) alleges the state law basis for the Attorney General's standing to seek judicial remedies for fraudulent diversion of charitable assets held by religious entities. Such assets are deemed to be held in trust, and the corporations and individuals which control them are deemed to be trustees who hold legal but not beneficial title to them (Part II, infra, p. 18).

The complaint requests an accounting from individual defendants (and the for-profit corporate defendants) for their management of such assets, not on the basis of some abstract duty to do so upon state demand, *but because there is a specific necessity therefor*. Paragraph 12(a) of the complaint alleges that the individual and for-profit corporate defendants have diverted assets of the Church, College and Foundation to their own private benefit. (P.App. 17b.)

The state has not merely *alleged* a necessity for an accounting, it has produced evidence in state court *supporting* that allegation.[13]

Obviously, California, as well as other states, has a strong and compelling interest in forbidding fraudulent diversion

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[13]See Statement of the Case, pp. 1 to 11.

of corporate funds, whether or not the affected corporation is a church. Likewise, the state has a strong and compelling interest in ensuring that the officers of any corporation formed under state law obey the provisions of its articles of incorporation and state statutes requiring that the corporation be controlled by a lawfully selected board of directors and not by the individual fiat of one man. These are neutral principles of law and are applicable in the same manner to religious corporations as they are to secular ones. (See *Jones v. Wolf* (1979) ..... U.S. ..... 99 S.Ct. 3020; *Presbyterian Church v. Hull Church* (1969) 393 U.S. 440, 449.) Thus, the mere filing of an enforcement action by a state attorney general seeking to protect such compelling state interests can violate no First Amendment rights.

Neither does the relief requested in the instant suit go beyond that necessary to protect such compelling state interests. The instant suit prays for the equitable remedy of an accounting by the church as well as the other charitable corporations and individual defendants, and any equitable relief which the accounting shows is necessary to make the Church, College and Foundation whole and ensure against fraudulent diversions of assets in the future. Such relief is necessary to advance compelling governmental interests (correction of fraud and violation of state corporation laws). For example, much of the alleged fraud in this case consists of transactions between Stanley Rader, or businesses controlled by him, and the Church, College or Foundation.[14]

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[14]Under the law applicable when the said transactions occurred, such self-dealing transactions by fiduciaries are absolutely prohibited. (Cal. Civ. Code, Secs. 2228-2235.) Section 2234 makes any such transaction a ". . . fraud against the beneficiary of a trust." California courts hold that such prohibitions apply not only to trustees of charitable trusts but to officers and directors of charitable corporations as well. See, e.g., *People v. Larkin* (N.D. Cal. 1976) 413 F.Supp. 978, 981-982; *Lynch v. John M. Redfield Foundation* (1970) 9 Cal.App.3d 293, 301.

Under these circumstances, of course, all of the records of such transactions are either in the possession of Rader or the charities. With few exceptions, there would be no other sources for such evidence. If such records are barred from view, it would be impossible to determine the extent of the fraud and therefore impossible to secure adequate relief. For example, Rader testified that he did not know whether the Church put $500,000 or $800,000 into the Beverly Hills home to which he took title and which ultimately sold for $1.8 million, pocketing the proceeds. (R.App. 10-11.) This information is contained in Church financial records. Without an accounting from those records it will be impossible to determine the full extent to which the Church was damaged by this unconscionable transaction.

Rader himself refuses to answer questions upon deposition. His refusal to answer questions and to account is itself wrongful conduct for a fiduciary, and it emphasizes the necessity of examining the financial records of the charitable corporations, which it is alleged he controls, in order to determine the extent of his wrongdoing.

Moreover, mere examination and copying of financial documents and questioning of witnesses to financial transactions can have little effect on either the religious practices or administration of the church. Whatever minor imposition this may present to the custodians of church financial records and to church employed witnesses who have knowledge of financial transactions, is far outweighed by the governmental interest in correcting fraudulent diversion of corporate assets. Moreover, the burden upon religious practices would certainly be far greater if this remedy were not available. For there would then be no way to recover such misappropriations on behalf of religious entities.

This Court has approved far more extensive burdens upon individual's rights to practice their religions in situations where such burdens were necessary to advance substantial governmental interests. In *Gillette v. United States* (1971) 401 U.S. 437, it was held that so-called selective conscientious objectors who objected only to the Vietnam War as an unjust war, rather than to war in any form, may constitutionally be required to perform military service. The court held, at page 462, that "incidental burdens [on the exercise of religion may be] justified by substantial governmental interests." In *Johnson v. Robison* (1974) 415 U.S. 361, it was held that a conscientious objector who performed alternate civilian service in lieu of military service may constitutionally be denied veteran's educational benefits by the United States Government. In *Braunfield v. Brown* (1961) 366 U.S. 599, a Pennsylvania law requiring businesses to close on Sundays was upheld against the claim that it was unconstitutional as applied to merchants whose religion observed Saturday as the Sabbath and whose religious beliefs compelled them to close their businesses on Saturday. The state's interest in obtaining one day a week of entire peace and quiet was held to outweigh the burden upon the Sabbaterian merchants who were forced to close their businesses both Saturday and Sunday, to their great economic detriment. (366 U.S. at 607.) Finally, in *Prince v. Massachusetts* (1944) 321 U.S. 158, it was held that a state child labor law forbidding minors from selling literature in public places did not violate the First Amendment rights of a child and her guardian where the guardian furnished the minor with religious literature and permitted her to distribute the same on the streets. It was held that the state's interest in protecting children outweighed the consequent burden upon a religious practice (321 U.S. at 170).

III.

The First Amendment Does Not Require That Courts Refuse to Enforce the Provisions of a Church's Own Corporate Charter.

A principal purpose of the instant suit is to enforce the provisions of the church's own Articles of Incorporation against the officers who have violated them. Such provisions include Article II(d) (R.App. 90) which provides that the corporation is not formed for the private profit of any member, and Article IV (R.App. 90), which requires that the business of the corporation be governed by a board of directors (rather than by individual fiat, which the trial court found to be the case with Petitioner Church herein). (R.App. 23.)

Incredibly, petitioners argue that the state's demand that the church corporation be governed in accord with the dictates of its own charter is an attempt to *restructure* the form of church governance from hierarchial to congregational (Petition, p. 40). Such a claim in itself is an admission that management has not in fact governed the corporation according to its own rules.[15]

If such provisions cannot be enforced by legal process, then no church would be free to incorporate with any expectation that the terms of its articles would be effective. These terms of course are not imposed upon the church by the state, but voluntarily adopted by it as the rules which

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[15]The state seeks also to remove individual defendants who may be found to have committed fraud from holding any office or employment in any of the subject charitable corporations, under the well-settled equitable principle that the court may remove trustees who are guilty of breaching their trust. We do not suggest that the court may remove any person from any ecclesiastical position which he may hold. However, if he misuses church funds such a person may constitutionally be disabled from doing so again by being removed from corporate office.

govern its existence as a temporal entity. Having voluntarily chosen to be governed by those rules, corporate officers have no right to exemption from their enforcement. (Compare *Hamilton v. Regents* (1934) 293 U.S. 245, in which this Court held that having voluntarily chosen to attend a state university, students did not have a right under the 1st Amendment to be exempted from university-required military training classes because the student's religious beliefs were opposed to participating therein. Of course, in the instant case, not even petitioners claim that diversion of church assets to private profit is sanctioned by any religious doctrine or belief.)

The courts have uniformly enforced a church's own arrangements for control of church property. Thus, state statutes purporting to authorize local congregations of a hierarchial church to withdraw from the parent church and take church property with them have been held unconstitutional. (See *Northside Bible Church v. Goodson* (5th Cir. 1967) 387 F.2d 534, 537-538.) Similarly, this court invalidated a New York statute designed to transfer control of a cathedral from the parent church headquartered in Russia to a local organization of the same church. (*Kedroff v. St. Nicholas Cathedral* (1952) 344 U.S. 94.)

Just as civil courts must enforce a church's ecclesiastical rules determining in whom church law places control over a cathedral building, they must enforce the Articles of Incorporation adopted by the same church to govern its temporal affairs. Failure to do so would impede religious liberty in both instances in exactly the same way, by rendering ineffective the rules the church has voluntarily adopted for the governance of its affairs. In neither case does such enforcement constitute either a decision of a question of religious doctrine, or a forbidden entanglement in religious affairs.

Where the rule to be enforced is a prohibition against diversion of church assets to private profit, the state interest in enforcement is much greater than that of merely providing a forum for the settlement of a dispute concerning who has the right to control church property. The state interest is nothing less than preventing the dissipation of such assets altogether. And the policy behind state law that charitable (including religious) assets are held in trust (see argument, *supra*, pp. 17-22) makes that interest even stronger.

Petitioners' contention that "intra-church transactions" (such as Mr. Rader's employment contract) are somehow exempt from state law fiduciary standards (Petition, p. 37)[16] conflicts with the approach this Court has taken to the resolution of church property disputes. Such disputes (which typically concern fights for control of church assets between factions with religious doctrinal differences—See *Watson v. Jones*, 13 Wall. 679) are at least as much "intra-church" matters as Rader's unconscionable employment contract (to which the Church agreed without benefit of independent legal counsel) or his egregious transfer to himself and subsequent sale of a $1.8 million dollar church-owned mansion. (See Statement of the Case, *supra*, p. 2.) But they are nevertheless resolved by the courts through the application of "neutral principles of law." See *Jones v. Wolf* (1979) ..... U.S. .....,) 99 S.Ct. 3020; *Presbyterian Church v. Hull Church* (1969) 393 U.S. 440 at 449.

Petitioners also contend that the state does not seek to apply "neutral principles of law" to this case because it

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[16]Certainly their speculations that "arms length bargaining may be wholly alien to intra-church relationships" (Petition, p. 37) and that there may be "fiduciary strictures . . . prevailing within the Church" which vary from those "preferred by . . . the state" (Petition, p. 39) are both unsupported by the record and in conflict with Article II(d) of its Articles of Incorporation (See p. 36, *supra*).

ignores the alleged wishes of church members whom it does not allege disapprove of the way in which church leaders have spent its assets (Petition, p. 39). (In so contending, petitioners ignore the fact that the State does allege that church leaders have failed to fully account to anyone for such expenditures (P.App. 17b), and that evidence indicates self dealing transactions occurred without even Board of Director knowledge or approval (See Statement of the Case, *supra*, p. 6).) This claim is truly ironic in the light of the fact that the Superior Court found that "Mr. Armstrong has apparently taken the position that he can do what he pleases [with church affairs] without consulting with anyone else." (See Statement of the Case, *supra*, p. 6.) For it presupposes what church leaders deny, that church members are entitled to any voice in the governance of its affairs.

IV.

The Conduct of the Lawsuit Has Not Violated Petitioners' Fourth Amendment Rights.

Petitioners argue that the alleged "initial illegality" of the receivership "taints the discovery orders upheld below (Petition, pp. 41-43),[17] implying that the State's subsequent discovery requests were shaped by "reviewing information obtained by the . . . receiver' " (Petition, p. 42). But that argument fails because (1) the receiver's examination of financial documents intruded upon no reasonable expecta-

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[17]That contention assumes the applicability of the exclusionary evidence rule to civil proceedings. But this Court has so far refused to apply the exclusionary rule in civil cases. In that regard Justice Blackmun, speaking for the majority in *United States v. Janis* (1976) 428 U.S. 433, 447 stated that "(i)n the complex and turbulent history of the (exclusionary) rule, the Court never has applied it to exclude evidence from a civil proceeding, federal or state." Again in *United States v. Calandra* (1973) 414 U.S. 338, 348 the Court stated that the exclusionary rule has "never been interpreted to proscribe the use of illegally seized evidence in all proceedings or against all persons."

tion of privacy, and (2) the receiver's actions were authorized by valid legal process supported by a strong and adequate showing of need.

The Fourth Amendment to the United States Constitution prohibits only *unreasonable* searches and seizures. "Whether the government's activity is considered a 'search' depends upon whether the individual's reasonable expectations of privacy are disturbed." (*Davis v. U.S.* (1967) 413 F.2d 1226, 1232 (5th Cir. 1969), citing the test formulated in *Katz v. U.S.* (1967) 389 U.S. 347, which first defined reasonableness for Fourth Amendment purposes in terms of the individual's expectation of privacy.)

A trustee has the duty to give full and accurate information concerning trust assets to the beneficiary and to permit him to examine the trust property and accounts. (*Union Trust Company of San Diego v. Superior Court* (1938) 11 Cal.2d 449, ...; *Scott On Trusts* (3d ed.) § 173.)

Accordingly in *Strauss v. Superior Court* (1950) 36 Cal.2d 396, the California Supreme Court upheld the validity of a trust beneficiary's subpoena duces tecum to the trustee compelling him to produce all trust financial records for a period of 15 years; this in a proceeding to perpetuate testimony at a time when the beneficiary had not even filed an action accusing the trustee of any wrongdoing. The Court based its holding on the right of the trust beneficiary to inspect all trust books and records. (36 Cal.2d at 401.) Moreover, the Court rejected the contention that such a broadly worded subpoena constituted an unreasonable search and seizure in violation of the Fourth Amendment. (36 Cal.2d at 403.) It is therefore settled law in California that a trustee has neither a legal right, nor a reasonable expectation, of privacy in the books and records of the trust vis-a-vis the trust beneficiary or his representative. If there is no such reasonable expectation of privacy in trust records

it follows that the beneficiary's inspection of such records does not constitute an unreasonable search and seizure within the meaning of the Fourth Amendment. (*Katz v. U.S.* (1967) 389 U.S. 347, 353; *Davis v. U.S.* (2d Cir. 1969) 413 F.2d 1226, 1232.)

The financial records of trustees have been traditionally subject to close scrutiny by courts of equity and by trust beneficiaries. In the case of a charitable trust, the state attorney general represents the beneficiary and indeed is the only party having legal standing to do so. (See Argument, *supra*, pp. 17-25.)

Even if the actions of the court appointed receiver in taking possession and commencing an audit of the financial books and records of the Church, College and Foundation were considered to be a "search," such actions nevertheless would comply with the requirements of the Fourth Amendment. The actions were authorized by valid legal process in the form of an ex parte order.[18] The issuance of such order ex parte was reasonable under the circumstances because it was supported by a showing of severe irreparable injury to the public interest; *i.e.*, the probability that charitable trust assets were being diverted to private benefit and that records of such diversion would be destroyed or hidden if defendants were given advance notice of the application for the order (see Statement of the Case, *supra*, p. 5, n. 4).

If there were any constitutional requirement for the legal equivalent of a warrant to support the actions of the receiver in this case, that requirement could be no more stringent

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[18]An ex parte order is clearly constitutionally permissible, even when it affects First Amendment rights. In *Zurcher v. Stanford Daily* (1978), ... U.S. ...., 98 S.Ct. 1970, 1983, where police obtained a warrant (ex parte) to search files of a newspaper, this Court specifically declined to "demand prior notice and hearing in connection with the issuance of search warrants."

than the showing required as a basis for civil searches by government administrative agencies. In civil inspections, such as this one:

> " 'Probable cause' to issue a warrant to inspect must exist if reasonable legislative or administrative standards for conducting an area inspection are satified with respect to a particular dwelling." (*Camara v. Municipal Court* (1967) 387 U.S. 523, 538.)

In applying a balancing test between the public need and the private right to be free from governmental intrusions, the Court in *Camara, supra*, stated that:

> "[b]ecause the inspections are neither personal in nature nor aimed at the discovery of evidence of crime, they involve a relatively limited invasion of the urban citizen's privacy." (*Id.* at 536-537.)

Likewise, in the instant case the public need to inspect charitable trust records has been shown to be compelling and the private interest infringed by such inspection, if any, is very minor. For example, "self protection" is one of the most important interests which underlie the Fourth Amendment freedom from unreasonable search and seizure. (See *Camara, supra*, at 530-531.) In the instant case, the Church, College and Foundation have no "self protection" interest in being free from an examination of their financial records, because it is clear that those entities are not charged with any violations of either criminal or civil laws. Indeed, the action is brought for the purpose of benefiting such corporations by halting fraudulent diversions of their assets.

In *Marshall v. Barlow's Inc.* (1978) 436 U.S. 307, 320, the Court confirmed that to obtain a warrant for a civil inspection it is sufficient that a government agency show only that "reasonable legislative or administrative standards for conducting an inspection are satisfied with respect to a

particular [place]." Moreover the court added that "if a valid public interest justifies the intrusion contemplated [by an inspection] then there is probable cause to issue a suitably restricted search warrant." (*Id.* at 323.)[19]

Conclusion.

For all of the above stated reasons, the petition should be denied.

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Respectfully submitted,

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[19]Even if the ex parte order appointing the receiver did not meet requirements for civil search warrants, a warrantless search would have been justified by the emergency circumstances of the instant case. A showing was made before the Superior Court that if an ex parte receiver were not appointed irreparable injury would occur to a compelling state interest. In such a circumstance a warrantless search would have been justified. For example, government seizure of unwholesome food and government compelled small pox vaccinations have been upheld against contentions that such actions constitute illegal searches or seizures in violation of the Fourth Amendment. (See *North American Cold Storage Company v. City of Chicago* (1908) 211 U.S. 306; *Compagnie Francaise v. Board of Health* (1902) 186 U.S. 380.) Similarly, in ruling that prejudgment garnishment of a civil defendant's wages without notice or hearing violated his right to due process of law, this Court observed that: "Such summary procedure may well meet the requirements of due process in extraordinary circumstances." (*Sniadach v. Family Finance Corporation* (1969) 395 U.S. 337, 339. See also *Randone v. Appellate Department* (1971) 5 Cal.3d 536, 556.)